

## **806 KAR 15:070. Annuity nonforfeiture.**

RELATES TO: 304.14-120, 304.15-365

STATUTORY AUTHORITY: KRS 304.2-110, 304.15-365(7)

NECESSITY, FUNCTION, AND CONFORMITY: KRS 304.2-110(1) authorizes the Executive Director of the Office of Insurance to promulgate administrative regulations necessary for or as an aid to the effectuation of any provision of the Kentucky Insurance Code, KRS Chapter 304. KRS 304.15-365(7) authorizes the executive director to promulgate administrative regulations to implement KRS 304.15-365(6) the statute and to provide for further adjustments to the calculation of minimum nonforfeiture amounts for contracts that provide substantive participation in an equity index benefit and for other contracts for which the executive director determines adjustments are justified. This administrative regulation establishes requirements to implement the provisions pertaining to annuity nonforfeiture in KRS 304.15-365(4).

Section 1. Definitions. (1) "Basis" means:

(a) If used in the context of an initial or redetermination method, the specified period over which an average is computed that produces the value of the five-year Constant Maturity Treasury (CMT) Rate; or

(b) If used in the context of equity-indexed benefits, the point in time used for establishing the parameters that:

1. Are incorporated into the calculation of the value of the equity-indexed options; and
2. Include the risk free rate, dividend yield, index volatility, and prior index values if the option is path dependent.

(2) "Equity-indexed benefits" means a benefit that:

(a) Is in an annuity contract in which the value of the benefit is determined using an interest crediting rate based on the performance on an equity-based index and contract parameters; and

(b) Does not include variable benefits of separate account variable annuities and indexed guaranteed separate account contracts purchased by institutional buyers.

(3) "Executive director" is defined in KRS 304.1-050(1).

(4) "Index term" means each period of time until the next indexed interest crediting date.

(5) "Initial method" means the basis upon which the initial nonforfeiture rate is established and the period for which it applies and which may last for the entire duration of the contract.

(6) "Initial nonforfeiture rate" means the nonforfeiture rate applicable at contract issue.

(7) "Minimum nonforfeiture amount" means the amount determined pursuant to KRS 304.15-365(4)(a).

(8) "Modal period" means the period the company specifies during which the current nonforfeiture rate will remain fixed.

(9) "Nonforfeiture rate" means the interest rate established in KRS 304.15-365(5).

(10) "Redetermination method" means the redetermination date, basis, and period for all future redetermination nonforfeiture rates.

Section 2. Basis Applicability. The same basis shall apply to equity-indexed benefits and nonequity-indexed benefits, if any.

(1)(a) The basis may use a specified period that is determined by the level of change in the CMT rate, or another date-dependent methodology adopted by the National Association of Insurance Commissioners and in compliance with this administrative regulation.

(b) A specifically excluded method is a method that shall define the nonforfeiture rate as the lowest rate in a specified time period.

(c) A method based upon changes in CMT levels shall move up or down in an identical manner with changes in interest rates, subject to KRS 304.15-365(5).

(2) If the basis uses a specified period determined by the level of change in the CMT rate:

(a) The nonforfeiture rate applicable if this subsection is first utilized for a contract form shall be determined by a method using a specified period or a date dependent methodology in compliance with this administrative regulation.

(b)1. A symmetrical range shall be defined that will determine if the rate shall be updated.

2. The maximum allowable range shall be plus or minus fifty (50) basis points.

(c) At the beginning of each modal period, a potential nonforfeiture rate shall be calculated using the method in paragraph (a) of this subsection, without incorporating caps or floors.

(d) If the difference between the potential nonforfeiture rate and the current initial nonforfeiture rate is less than or equal to the range, the current nonforfeiture rate shall not be updated.

(e) If the difference between the potential nonforfeiture rate and the current nonforfeiture rate is more than the range, the current nonforfeiture rate shall be updated to be equal to the potential nonforfeiture rate adjusted for rounding and caps or floors.

Section 3. Initial Method. (1) The initial method shall be filed with the executive director.

(2)(a) Changes to the initial method shall be allowed once per calendar year.

(b) Changes to the initial method shall be filed with the executive director in accordance with KRS 304.14-120.

(c) A change in initial method would be applicable only to new contracts or new certificates issued subsequent to the effective date of the change in method.

(3) The initial method shall not be required to be disclosed in the contract form.

(4) The initial nonforfeiture rate shall not be required to be disclosed in the contract form unless redetermination is used.

(5) The minimum nonforfeiture parameters shall not be required to be disclosed in the contract unless they are utilized in the calculation of the guaranteed minimum value of the contract.

Section 4. Redetermination Method. (1) If redetermination is used, the method shall be disclosed in the contract form or certificate.

(2) Changes in the redetermination method for future issues or certificates shall be filed in accordance with 304.14-120.

Section 5. Nonforfeiture Rate and Minimum Nonforfeiture Amount. (1) An annuity contract or certificate without an equity-indexed benefit shall have one (1) nonforfeiture rate and one (1) minimum nonforfeiture amount applicable to the entire contract.

(2) An annuity contract or certificate with equity-indexed benefits may have more than one (1) nonforfeiture rate applicable to the contract or certificate subject to the following:

(a) If the contract has a non equity-indexed benefit, the nonforfeiture interest rate applicable to the non equity-indexed benefit shall be determined in compliance with KRS 304.15-365(5) without any consideration of any equity indexed feature.

(b) If an additional reduction is elected for equity-indexed benefits, reduced nonforfeiture interest rates may apply to each equity-indexed benefit for which the additional reduction is elected in compliance with KRS 304.15-365(6) and Section 5 of this administrative regulation.

(c) The minimum nonforfeiture amount for the contract shall be determined by calculating a nonforfeiture amount, without any reduction for indebtedness to the company on the contract including interest due and accrued on the indebtedness, for each equity-indexed and non equity-indexed benefit using the nonforfeiture interest rates described in this subsection, summing

the results, and then deducting any indebtedness to the company on the contract including interest due and accrued on the indebtedness.

(d) If contract value is transferred:

1. From a benefit, the benefit's minimum nonforfeiture amount shall be reduced by the benefit's minimum nonforfeiture amount prior to the transfer multiplied by the proportion of the benefit's contract value that is transferred;

2. To a benefit, the benefit's minimum nonforfeiture amount shall be increased by the sum of all reductions in minimum nonforfeiture amounts determined pursuant to subparagraph 1 of this paragraph, multiplied by the proportion of total contract value that is transferred to that benefit; or

3. For purposes of the calculations specified in subparagraphs 1 and 2 of this paragraph the contract value shall first be reduced by any fees associated with the transfer.

(e) In the case of a withdrawal from a benefit in which the amount of withdrawal exceeds the benefit's nonforfeiture amount, the insurer shall treat the excess withdrawal in a manner at least as favorable to the contract holder as deducting the excess withdrawal from the nonforfeiture amounts of other benefits in order from lowest to highest nonforfeiture interest rate.

(f) A contract charge or premium tax paid by the company shall be allocated to a benefit's minimum nonforfeiture amount based on the percentage of that benefit's contract value to the total contract value.

Section 6. Equity-indexed Benefits. (1) If a company chooses to take the additional reduction for an equity-indexed benefit, the company shall prepare a demonstration showing compliance with KRS 304.15-365(6).

(2) To demonstrate compliance a company shall:

(a) Calculate the annualized option cost for the equity-indexed benefit in the form of basis points for the entire index term as of the beginning of the index term.

1. In making the calculation, a company shall:

a. Use the equity-indexed benefit's guaranteed product features;

b. Use a basis representative of the point in time at the beginning of the current index term for the option cost. The company shall not change this basis during the index term; and

c. Calibrate the method and parameters for the option cost to capital markets based option pricing.

2. A company shall not make adjustments for persistency, death, or utilization.

(b) Be eligible to take a reduction equal to the lesser of 100 basis points or the annual cost basis value, if the annualized option cost for the equity-indexed benefit is twenty-five (25) basis points or more, and the equity-indexed benefit shall provide substantive participation under KRS 304.15-365(6).

(c) Prepare an actuarial certification signed by a member of the American Academy of Actuaries that the reduction complies with KRS 304.15-365(6) at the time that the contract form is filed and submitted.

(d) Annually prepare an actuarial certification in accordance with KRS 304.15-365(6) signed by a member of the American Academy of Actuaries with regard to ongoing compliance and submit it in conjunction with the filing of the annual statement.

(3) If the additional reduction of up to 100 basis points for equity-indexed benefits has been inappropriately taken, the executive director shall require the recalculation of all values for all affected policyholders without all or part of the additional reduction.

Section 7. Effective Date. The requirements, implementation, and enforcement of this administrative regulation shall begin on January 1, 2008. (33 Ky.R. 4311; Am. 34 Ky.R. 304; 746;

eff. 11-2-2007; Crt eff. 2-26-2020.)